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SURFACE TRANSPORTATION BOARD

DECISION

STB Finance Docket No. 33726

WESTERN COAL TRAFFIC LEAGUE
v.
UNION PACIFIC RAILROAD COMPANY

Decided: November 27, 2000

In this proceeding, Western Coal Traffic League (WCTL or petitioner) complained that the Union Pacific Railroad Company (UP) improperly reported as ordinary operating expenses in its 1997 Annual Report R-1 (R-1) the expenses that UP had incurred to address widespread congestion on its Houston/Gulf Coast region lines following its merger with the Southern Pacific Transportation Company (SP).[1] By decision served May 12, 2000 (May Decision), we determined that UP's accounting treatment of these expenses, and of certain other expenses that it had incurred in connection with the merger, was consistent with our Uniform System of Accounts (USOA) and generally accepted accounting principles (GAAP), and we dismissed WCTL's complaint.[2]

On June 1, 2000, WCTL filed a petition for reconsideration of that portion of the May Decision upholding UP's ordinary-expense treatment of its congestion-related expenses. Relying as it did earlier on Amerada Hess Pipeline Co. v. FERC, 117 F.3d 596 (D.C. Cir. 1997) (Amerada Hess), WCTL renews its argument that the Houston/Gulf Coast service problems were of such degree that, pursuant to the USOA and GAAP, we should require UP to restate its R-1

[1] Union Pac. Corp.—Control & Merger—Southern Pac. Corp., 1 S.T.B. 233 (1996), aff'd sub nom. Western Coal Traffic League v. STB, 169 F.3d 775 (D.C. Cir. 1999).

[2] WCTL had also challenged (1) UP's determination to classify as ordinary expenses various merger-related restructuring expenses that it had incurred when it acquired SP (severing, relocating, and re-training its own employees, rationalizing its facilities, and upgrading equipment); and (2) its classification of certain SP restructuring expenses that it had assumed in connection with the acquisition as liabilities, which it treated as part of its purchase price of SP and included in its valuation of SP's assets. We found that UP properly accounted for these items as well.

report so as to classify these expenses as unusual or infrequent.[3] UP and the Association of American Railroads (AAR), as amicus curiae, replied. We deny the petition.

BACKGROUND

Under the USOA, 49 CFR 1200-1201, rail carriers are to report expenses as "unusual" when they arise from events that "possess a high degree of abnormality" and are "of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities" of rail carriers. Expenses are to be reported as "infrequent" when they arise from events that "would not reasonably be expected to recur in the foreseeable future." 49 CFR 1201, General Instruction (Inst.) 1-2(d)(1). As we explained in our May Decision, at 3-4, the costs that UP experienced during its service breakdown — costs associated with borrowing rail cars from other carriers (car hire); acquiring new locomotives; hiring crews; performing maintenance and repair; and dealing with customer claims — are normal costs of railroading, and railroads typically have treated these types of expenses, when incurred to address the congestion and service disruptions that regularly arise in railroading, as ordinary operating expenses, not unusual or infrequent expenses.

We rejected WCTL's argument that the breadth and severity of the congestion over UP's system that was spawned by the Houston/Gulf Coast service breakdown warranted a different accounting treatment for UP's congestion-related expenses. We observed that, unlike the Exxon Valdez Alaska oil spill addressed by the Federal Energy Regulatory Commission (FERC) in Amerada Hess, the expenses prompted by the service crisis here were not the result of any one event, but rather were caused by a confluence of several events and circumstances — derailments, maintenance, a major traffic embargo, severe weather, and traffic surges — not uncommon to railroading.[4] Further, while there was no doubt as to the broad impact of the

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[3] WCTL's objective is to have UP place these expenses in different accounts or otherwise segregate them so that they would not be counted in determining UP's variable costs under our Uniform Railroad Costing System (URCS). May Decision, at 2 n.8, 10. Not doing so, WCTL argues, would result in overstating UP's variable costs for its 1997 services and, together with the limitations on our jurisdiction under 49 U.S.C. 10707(d), work to decrease the amount of traffic potentially subject to our rate reasonableness authority. Id. at 1 n.2.

[4] May Decision, at 5-6. The precipitating events of the service crisis, involving several railroads at various locations in and near Houston and other parts of Texas and the Gulf Coast, included: derailments on SP mainline and terminal yardtrack in and around the Houston terminal; line curfews for maintenance imposed by BNSF on the eastern segment of the former SP Houston-New Orleans mainline over which UP operated; the backup and eventual embargo of Mexico-bound traffic at the international gateway at Laredo, TX; SP line washouts in Texas and Arkansas from unusually bad weather; traffic backups in Texas due to damage to connecting CSX lines from Hurricane Danny; and significant surges in demand for rail service due to the (continued...)

service crisis, we explained that, in accounting for its associated expenses, the magnitude, duration and geographic scope of the service crisis are not the controlling considerations. Rather, to classify expenses as unusual or infrequent under the USOA and GAAP, they must arise from events that are largely unique, unrelated, or unlikely to recur in a railroad environment. The causal events of the Houston/Gulf Coast service disruptions, we found, were clearly not of that character. May Decision, at 4-6.[5]

In its petition for reconsideration, WCTL largely revisits its previous arguments, contending that Amerada Hess requires us to consider the magnitude of the service crisis; that UP's accounting deconstruction of the service crisis into a series of common railroading occurrences improperly evades that requirement, misapplies USOA and GAAP, and wrongly masks what was a discrete and unprecedented transportation event; and that permitting UP to report its congestion-related expenses as ordinary operating expenses and include them in its URCS costs violates our obligation under 49 U.S.C. 10101(13) to ensure the availability of accurate cost information in rate proceedings.[6] Petitioner's arguments, however, remain unpersuasive.

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[4](...continued)
expanding economy. Id. at 5 n.14; see also AAR Opposition, at 5. The congestion around Houston produced by these events was also exacerbated by the unusual and cramped configuration of the Houston terminal — a configuration of tracks and yards at grade that, even in normal circumstances, often required traffic-delaying switching operations on mainline track — plus the deteriorating state of SP's existing infrastructure and service generally, which was a primary basis for the Board's approval of UP's acquisition of SP. See Union Pac. Corp.—Control & Merger—Southern Pac. Corp., Finance Docket No. 32760 (Sub-No. 26) (STB served Dec. 21, 1998) (Houston/Gulf Coast Oversight), at 5, 24-25 n.46 (citations omitted); Joint Petition for Service Order, STB Service Order No. 1518 (STB served Feb. 17, 1998), at 5-7.

[5] WCTL had also suggested that, by formally describing its congestion-related expenses in notes to the R-1, UP had already recognized the uniqueness of the service crisis and, to be consistent, should segregate these expenses alternatively as "special charges." We explained, though, that for purposes of full disclosure, carriers often use notes in their financial statements to further explain already accounted-for revenue and expense items. More importantly, however, we found that even if UP had classified the congestion expenses as special charges, that would not have required UP to exclude these expenses from its 1997 URCS variable cost determination. We explained that special charges are often related to normal rail operations, and that so long as they are — as we found UP's congestion-related expenses were here — they may be properly included in URCS costs. May Decision, at 10-11.

[6] Petitioner also asserts that we erred in rejecting its alternative request that UP reclassify its congestion expenses as special charges (see note 5), but it does not challenge this aspect of the May Decision on reconsideration. Petition, at 2 n.1.

DISCUSSION AND CONCLUSIONS

In authorizing us to prescribe a uniform accounting system for rail carriers, Congress directed us "to the maximum extent practicable" to conform to, and to administer any system that we adopt in accordance with, GAAP. 49 U.S.C. 11142, 11161, 11164. Under GAAP, an event or transaction is "presumed to be an ordinary and usual activity of the reporting entity" and accounted for in the income and expenses from operations "unless the evidence clearly supports its classification as an extraordinary item." Accounting Principles Board (APB) Opinion No. 30 (APB-30), ¶ 19. Extraordinary items are those that account for activities that are unusual and infrequent, and those terms are defined (APB-30, ¶ 20) as follows:

> *Unusual nature*–the underlying event or transaction should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the entity, taking into account the environment in which the entity operates.
>
> *Infrequency of occurrence*–the underlying event or transaction should be of a type that would not be expected to recur in the foreseeable future, taking into account the environment in which the entity operates.

The APB goes on to explain that "the environment in which an entity operates" is a "primary consideration" in determining whether an underlying event is unusual, and likewise should play a significant role in determining an event's infrequency. APB-30, ¶¶ 21, 22. That is so, the APB explained (id. at ¶ 22), because

> a specific transaction of one entity might meet the criterion and a similar transaction of another entity might not because of different probabilities of recurrence. The past occurrence of an event or transaction for a particular entity provides evidence to assess the probability of recurrence of that type of event or transaction in the foreseeable future. By definition, extraordinary items occur infrequently. However, mere infrequency of occurrence of a particular event or transaction does not alone imply that its effects should be classified as extraordinary. An event or transaction of a type that occurs frequently in the environment in which the entity operates cannot, by definition, be considered extraordinary, regardless of its financial effect.

The USOA definitions of unusual and infrequent items, 49 CFR 1201, Inst. 1-2(d) (May Decision, at 3), are virtually identical to those under GAAP. Thus, it is clear that, in considering whether to account for expenses as unusual or infrequent, the USOA and GAAP direct rail

carriers to focus on the fundamental nature of the events in question — not their magnitude — and we acted properly in applying our accounting rules in that way. Doing so, and finding that the triggering events and effects of the service crisis in the Houston/Gulf Coast region were not uncommon to railroading, we correctly concluded that, consistent with past industry practice, UP properly classified its associated costs in dealing with the congestion resulting from those events as ordinary operating expenses.

Amerada Hess, despite petitioner's continued insistence, does not require a different result. In that case, FERC examined the accounting treatment of certain litigation and settlement costs incurred as a result of the 1989 grounding of the Exxon Valdez oil tanker and the discharge into Prince William Sound, Alaska of millions of gallons of oil.[7] FERC determined that the vast scale of the oil spill required that these costs be classified not as ordinary business expenses, but as extraordinary items. In affirming FERC's decision, the D.C. Circuit concluded that it was not unreasonable for FERC to consider the oil spill's magnitude under the USOA because the spill was an event that constituted "a difference not just of degree but of kind."[8] Amerada Hess, 117 F.3d at 603.

The court's decision, however, should not be read to extend beyond the particular circumstances that it addressed. Under the relevant deferential standards of review that the court applied, its role was only to examine whether FERC's interpretation and application of the USOA in the context of Amerada Hess — and the weight that FERC assigned to the cause and size of the single event at issue — was a reasonable one. Thus, while it may be instructive, Amerada Hess does not — and should not — tell us how we should act in applying the USOA to

[7] This case made its way to FERC because initial responsibility for the clean-up of the oil spill was assumed by Alyeska Pipeline Service Company, the operator of the Trans-Alaska Pipeline System (TAPS). Although Exxon subsequently reimbursed Alyeska for the clean-up costs, Alyeska incurred almost $120 million in additional costs for settling claims against it related to the spill. Alyeska's joint owners, the oil pipeline carriers who also jointly owned TAPS, each paid a proportionate share of the settlement expenses and then filed tariff rates with FERC to recover those costs in higher pipeline rates. The State of Alaska protested, arguing that a prior FERC-approved agreement between the TAPS carriers and the State only permitted rate recovery of ordinary operating expenses and not, as the State urged, extraordinary items like the settlement costs at issue. FERC agreed and rejected the tariffs. See Amerada Hess, 117 F.3d at 599-600.

[8] FERC inherited the USOA of our predecessor, the Interstate Commerce Commission (ICC), upon Congress' 1977 transfer to FERC of the ICC's authority over oil pipelines, and FERC has retained the USOA largely intact. FERC's USOA is set forth at 18 CFR Part 352. Id. at 600-01.

specific accounting situations involving railroads, the industry that Congress has entrusted us to oversee.[9]

We cannot say what we would do if we had a case like Amerada Hess before us. But we do not need to speculate as to that question now because the service crisis presents a much different set of circumstances. Petitioner's arguments that we have ignored other more general statements regarding the "unprecedented" scale of the Houston/Gulf Coast service (Petition, at 8-9) continue to miss the essential point that, for accounting purposes, the service crisis was not a single event. Instead, it was a situation that arose from numerous events, many of which were unrelated[10] and none of which was so significant in scale or unique in railroading as to be extraordinary.[11] As a result, unlike the expenses arising from the grounding of the Exxon Valdez, it would be difficult to attribute UP's expenses to end the congestion and restore fluid

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[9] The court implicitly recognized this when it dismissed the argument that FERC was not entitled to judicial deference because it had not promulgated the USOA, observing that deference was due because Congress had delegated to FERC exclusive oversight of oil pipelines. Amerada Hess, 117 F.3d at 601. Clearly, Amerada Hess does not suggest the contrary notion that the Board should be afforded less deference than FERC on review of our subsequent interpretation and application of the USOA to railroad matters that are committed to our exclusive oversight. Not only would that be inconsistent with the entity-by-entity accounting approach envisioned by GAAP (APB-30, ¶ 22), but it would undermine the fundamental principle, reaffirmed recently by the court in Buffalo Crushed Stone, Inc. v. STB, 194 F.3d 125, 128 (D.C. Cir. 1999), that an agency's interpretation of the regulations governing its delegated field merits even greater deference than usual.

[10] See supra note 4; see also May Decision, at 5-6. In an effort to tie all of the precipitating events together, WCTL attempts to portray the service crisis as a "direct consequence" of UP's "ill-conceived" merger with SP. Petition, at 2. But as we determined previously, rather than causing the service crisis, UP's implementation of the merger in Texas — and its integration and absorption of a weak and deteriorating SP system — effectively marked the end of it. Houston/Gulf Coast Oversight, at 5, 11, 22-23.

[11] Even if — notwithstanding our view of proper accounting practices — we were to look at the service crisis as a whole, it would not measure up to the Alaska oil spill, which was far beyond any reasonable notion of an ordinary event. As the court itself noted, the Exxon Valdez incident was "the only spill from a tanker transiting Prince William Sound in 13,089 tanker calls," and this oil spill involved nearly 11 million gallons of oil, one that dwarfed to an almost infinite degree any previous spills in the sound (typically involving less than 10 gallons of oil). Amerada Hess, 117 F.3d at 603. Moreover, the grounding of the Exxon Valdez, as later determined, stemmed largely from acts of criminal negligence that cannot in any way be considered an ordinary part of oil tanker operations. May Decision, at 6 n.18; AAR Opposition, at 10-11.

operations to any one of the service crisis' precipitating events, and, as UP points out, the likely arbitrary allocations that would result from such an effort would not produce the accuracy and consistency that the USOA and GAAP require. UP Reply, at 6-7 and n.9.[12]

Further, our decision is consistent with the broader reality that periods of congestion and service disruptions of varying and often significant degrees, often stemming from multiple and unavoidable causes, are simply not uncommon in railroading. May Decision, at 5-6. Because the USOA and GAAP limit unusual or infrequent accounting treatment to highly atypical situations, the associated expenses to alleviate congestion have not, as a result, historically been aggregated into groups of distinct expenses and accounted for in that way. Thus, while the Houston/Gulf Coast service crisis was clearly a serious matter,[13] unlike the Alaska oil spill, it was not so different in kind that UP should reclassify its congestion-related expenses as unusual or infrequent.

We take seriously Congress' directive under 49 U.S.C. 10101(13) that we ensure the availability of accurate cost information in our regulatory proceedings, but the May Decision did not, as WCTL argues (Petition, at 11-13), violate that obligation in any way. In obtaining cost and revenue information for regulatory purposes, Congress has expressly directed us to conform our accounting rules used to report that information to GAAP to the maximum extent practicable. 49 U.S.C. 11164. Consistent with GAAP, the USOA permits the identification of expenses as unusual or infrequent only if they flow from events that are largely atypical, unrelated, or unlikely to recur in a rail environment. As we explained in the May Decision, and again here, the congestion-related expenses experienced by UP as a result of the Houston/Gulf Coast service crisis were not of that kind, but rather are more accurately accounted for as ordinary operating

[12] Complicating matters further, as we have noted, is that the expenses that rail carriers incur to address congestion — car hire, crew wages, locomotives, maintenance, customer claims, and the like — are the same kinds of expenses that they must incur normally. May Decision, at 4. Coupled with the multiple-event nature of the service crisis, there is no sound or practical way for UP to segregate congestion-related expenses as transitory, let alone distinguish expenses caused by the congestion from others made in the ordinary course of business to prevent congestion, enhance safety, or increase efficiency. See AAR Opposition, at 13-14.

[13] While there is no question as to the wide impact of the Houston/Gulf Coast service crisis, we pointed out previously that there have been numerous episodes of lengthy service disruptions that have imposed significant expenses upon rail carriers, May Decision, at 4 n.12, and, contrary to WCTL's argument (Petition, at 2) the $197 million in congestion-related expenses reported by UP do not differ in a "dramatic" way. Even if they did, however, the USOA and GAAP do not classify expenses based on the size of the expenses. Id. at 4; APB-30, ¶ 22.

expenses that, consistent with 49 U.S.C. 10101(13), may be used in constructing URCS costs.[14]

In sum, WCTL has not, as required by 49 CFR 1115.3(b)(2), demonstrated material error in the May Decision. Accordingly, we deny its petition for reconsideration.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

It is ordered:

1. The petition for reconsideration is denied.

2. This decision is effective December 30, 2000.

By the Board, Chairman Morgan, Vice Chairman Burkes, and Commissioner Clyburn.

Vernon A. Williams
Secretary

[14] We did not, as WCTL suggests (Petition, at 12), satisfy our duty under section 10101(13) by relying on an independent accounting firm audit finding UP in compliance with GAAP, but simply acknowledged the audit in the course of conducting our own analysis. May Decision, at 3.